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No. 516

In the Supreme Court of the United States

OCTOBER TERM, 1959

MARCAL PULP & PAPER, INC., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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Taxpayer-petitioner, a manufacturer of paper products, had an insurance policy which insured it against (1) property loss or damage caused by accident ("direct damage") and (2) losses sustained through prevention of business on the premises caused by accident ("use and occupancy") (R. 7a-8a).[1] In March, 1952, a crack appeared in a dryer roll which the taxpayer used in its paper-making

[1] "R." refers to the appendix in the court of appeals.

machine (R. 8a). Taxpayer made a claim therefor against the insurance company for $250,000, of which $154,000 was stated to be for "use and occupancy" loss (R. 9a). This claim was settled for $125,000, which taxpayer received in August, 1952 (R. 9a-10a). Although no allocation of this amount between direct damage and use and occupancy was agreed upon by the insurance company and the taxpayer, the insurance company, for purposes of its own records and for purposes of state insurance reserve requirements, allocated $25,000 to direct damage losses and $100,000 to use and occupancy losses (R. 9a).

In the summer of 1955, taxpayer replaced the old dryer roll (which had been repaired) with a new dryer roll which it had ordered shortly after the accident (R. 10a). The total cost of installing the new dryer roll was approximately $120,000 (R. 10a). In its amended income tax return for the fiscal year ended July 31, 1953, taxpayer reported additional income of slightly less than $5,000, representing the difference between the insurance proceeds received and the amount claimed as expended in replacement of the damaged property (R. 11a). The Commissioner determined, however, that only $25,000 of the $125,000 insurance settlement was to be allocated to "direct damage", and that the remaining $100,000 represented a payment for use and occupancy losses which was part of taxpayer's income (R. 13a).

The Tax Court sustained the Commissioner's determination. The court ruled (R. 17a) that the entire amount of the insurance settlement could not

be ascribed to the "direct damage" provisions of the contracts, and that "some allocation of the insurance proceeds is necessary." It stated (R. 16a) that "some expected losses of profit were taken into consideration when the parties agreed upon a compromise settlement"; and that taxpayer "gave up a portion of its claim in exchange for a partial reimbursement from Mutual [the insurance company] of both its direct damage and its use and occupancy losses." The court concluded (R. 17a) that the Commissioner's allocation of $25,000 to direct damage and $100,000 to use and occupancy losses was "reasonable in view of the cost and age of the old dryer roll" [2] and the taxpayer's failure "to present credible evidence of some more reasonable allocation."

In a *per curiam* opinion (Pet. A-1), the court of appeals stated that it "perceive[d] no error in the reasoning or the decision of the Tax Court," and it affirmed on the "thoughtful opinion" of that court.

Petitioner presents only the narrow question whether the Commissioner properly allocated the amount it received from the insurance company between "direct damage" and "use and occupancy" losses. As the Tax Court pointed out (R. 13a) in sustaining the Commissioner's determination, "[t]he question of allocation is peculiarly one of fact." The Tax Court fully reviewed and rejected all of petitioner's contentions, and its opinion sets forth the factual justification for the Commissioner's alloca-

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[2] The dryer roll was acquired in 1948 at a cost of $40,000. At the time of the accident, its depreciated basis was less than $32,000 (R. 11a).

tion. Petitioner's arguments rest on a construction of the insurance contract which was rejected by both courts below. Although it contends (Pet. 10-12) that the decisions below are in conflict with other cases in which unapportioned settlements have received allegedly different tax treatment, those cases all involved substantially different facts. The decision below, unanimously affirming the Tax Court, is correct, and the factual issues presented do not call for further review.

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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